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11 U.S.C. § 363(c)
11 U.S.C. § 507(b)
Superpriority

In re I.F. Rodgers & Sons and I.F. and Lorraine Rodgers

696-62478-aer11
696-62477-aer11

10/13/00 Alley Unpublished

Creditor was secured by real property and a cattle herd. DIP moved under § 363(c)(2) for authorization to use cash collateral to be generated from the sale of cattle. Creditor objected. The court granted the motion finding a sufficient equity cushion existed in the real property to provide the required adequate protection. The cash collateral generated was in fact used for the DIP's operations.

Subsequently, all of Creditor's collateral, including the real property, was liquidated. The "equity cushion" proved illusory, and Creditor sought superpriority treatment under § 507(b) for the amount of cash collateral used.

The court allowed § 507(b) treatment, holding the court's initial finding of an "equity cushion", and its implicit direction that the remaining collateral not be used, met the requirement that DIP "provide" adequate protection under § 507(b). Further, Creditor's claim met the other requirements of § 507(b) in that it was entitled to administrative treatment, and arose from use of the cash collateral.

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UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF OREGON

In Re the Administratively) Bankruptcy Case Nos.
Consolidated Estates of:) 696-62478-aer11
I.F. RODGERS & SONS and) 696-62477-aer11
I.F. RODGERS and LORRAINE RODGERS,)
Debtors.) MEMORANDUM OPINION¹

South Valley Bank has filed a proof of claim for \$157,711, arising from the debtor-in-possession's sale of cattle in which the Bank had a perfected security interest. I find that the Bank is entitled to have its claim for these proceeds treated as an administrative priority claim.

At the time this case was commenced the debtor-in-possession was indebted to the Bank for over \$900,000. The debt was secured by real property owned by the DIP, and a cattle herd. The DIP applied for an order permitting to sell the cattle and use the proceeds - which were also subject to the Bank's security interest - to support ongoing business operations. Over the Bank's objections the court

¹ This Memorandum is not intended for publication, and will not be posted on the Court's website.

1 entered an order permitting the sale and use of the resulting cash
2 collateral. The herd was sold at auction, and \$157,711 was
3 received. This entire amount was subsequently spent by the DIP on
4 operations in the 1997-98 season.

5 Subsequently the balance of the Bank's collateral was sold,
6 resulting in payment of about \$480,000. There remains unpaid
7 roughly \$420,000, far more than the amount of cash collateral used
8 by the DIP.

9 The proceeds of the sale of the Bank's collateral was itself
10 subject to the security interest, and was cash collateral, as that
11 term is defined by 11 U.S.C. § 363(a). Cash collateral may not be
12 used by a debtor-in-possession unless the secured party consents, or
13 the court, by order, permits such use. 11 U.S.C. § 363(c)(2). Use
14 may be authorized only upon a finding that the secured party has
15 been provided with adequate protection. Code § 363(e). Adequate
16 protection may consist of cash payments, additional or replacement
17 liens, or any relief providing the "indubitable equivalent" of the
18 secured party's interest, other than priority payment under
19 § 503(b)(1). See 11 U.S.C. § 361. The court found in this case
20 that the value of the real property exceeded the amount owed to the
21 bank, and that the resulting "equity cushion" was sufficient to
22 provide the adequate protection required to allow use of the
23 proceeds of the cattle sale. Accordingly, the sale was authorized
24 without any additional protection.

25 As it turned out, the equity cushion was illusory, and the
26 real property brought less than was owed. The bank was effectively

1 deprived of a valid security interest to the extent its collateral
2 was used by the DIP to operate. The question is, what remedy is
3 available when adequate protection fails?

4 Code § 507(b) provides:

5 If the trustee [or a debtor-in-possession - see
6 § 1107], under section 362, 363, or 364 of this title,
7 provides adequate protection of the interest of the
8 holder of a claim secured by a lien on property of the
9 debtor and if, notwithstanding such protection such
10 creditor has a claim allowable under subsection (a)(1)
11 of this section arisingfrom the use, sale or
12 lease of such property under section 363 of this
13 title....then such creditors claim shall have priority
14 over every other claim under such subsection.

15 In other words, the statutory remedy when cash collateral is
16 used for the benefit of the estate, and adequate protection measures
17 fail is to assign to the now unsecured claim priority over all other
18 § 507(a)(1) administrative claims - a "superpriority". In re Wise
19 Transportation, Inc., 148 B.R. 52, 54-55 (Bankr. N.D. Ok. 1992), In
20 re Quality Beverage Co., 181 B.R. 887 (Bankr. S.D. Tex. 1995).
21 Adequate protection is not restricted to any particular form, and
22 may be said to be "provided" by court recognition of an equity
23 cushion sufficient to protect the creditor's interest. When the
24 equity cushion is eroded, or proves to have been illusory, award of
25 a superpriority is appropriate. In re Kids Creek Partners, L.P.,
26 220 B. R. 963, 970 (Bankr. N.D. Ill. 1998).

27 One of the debtor's principals testified that all of the
28 proceeds from the sale of the cattle were used for the DIP's
29 operations. This means that the expenditures were for the direct
30 benefit of the estate. Resulting claims are entitled to priority

1 payment under § 507(a)(1). It is equally clear that, in the end,
2 the Bank's interest was not adequately protected by the existence of
3 excess cash value in other collateral. The court's finding that the
4 equity cushion provided adequate protection, and its implicit
5 direction that the remaining collateral not be used, amounted to a
6 provision of adequate protection for purposes of § 507(b).

7 It follows that the Bank is entitled to superpriority
8 administrative treatment of its claim for failure of adequate
9 protection, in the sum of \$157,711 pursuant to § 507(b). Counsel
10 for the Bank shall lodge an order to that effect.

11 The foregoing constitutes the court's findings of fact and
12 conclusions of law.

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15 FRANK R. ALLEY, III
16 Bankruptcy Judge
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